

JUL 1 1994

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of)	
)	
Implementation of Sections of)	MM Docket No. 93-2151 ✓
the Cable Television Consumer)	
Protection and Competition Act)	
of 1992: Rate Regulation)	
)	
and)	
)	
Adoption of a Uniform Accounting)	CS Docket No. 94-28
System for Provision of Regulated)	
Cable Service)	

COMMENTS OF BELL SOUTH

BellSouth Corporation and BellSouth Telecommunications, Inc. ("BellSouth") hereby offer comment in the captioned proceeding in response to the Commission's Report and Order and Further Notice of Proposed Rulemaking ("FNPRM"), FCC 94-39, released March 30, 1994, 59 Fed. Reg. 19066 (April 15, 1994.)

BellSouth supports the hierarchy adopted by the Commission for the regulation of the cable television industry. That hierarchy provides that where effective competition exists, no rate regulation is applicable. In the absence of effective competition, a benchmark/price cap approach provides the primary regulatory regime. A streamlined version of cost of service regulation is adopted only as a secondary approach.¹ This hierarchy imposes regulation only in the absence of effective competition, and

¹ FNPRM at para. 25.

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then only to the extent necessary to fulfill the Congressional mandate contained in the Cable Act of 1992.

BellSouth concurs with the Commission's determination that a pure price cap approach best meets the Congressional mandate to insure that rates for regulated cable services are reasonable.² A pure price cap approach is an effective means of regulating companies in a market where competition is emerging. With the convergence of cable television and telecommunications technologies, it is critically important that regulatory parity be achieved for these two industries, and that the regulatory regime provide the proper incentives for efficiency, capital formation and infrastructure development.³ A pure price regulation plan best achieves these goals.⁴ In the remainder of these comments, BellSouth will evaluate specific aspects of the Commission's regulation of cable television companies against a goal of pure price regulation.

For those cable operators electing cost of service regulation and for those operators that seek to adjust

² FNPRM at para. 4.

³ The Commission recognizes the need for regulatory parity between cable television companies and telephone companies in the FNPRM at para. 319.

⁴ While advocating a "pure" price cap regulatory model for both the cable television and telephone industries, BellSouth is mindful that the current price cap model applied to Local Exchange Carriers ("LECs") is far from ideal. BellSouth has made specific recommendations for change in the LEC price cap plan in its comments in CC Docket No. 94-1.

benchmark/price cap rates for affiliated programming costs, the Commission has adopted affiliate transaction rules patterned after those presently applicable to telephone companies.⁵

The existing affiliate transaction rules are codified as Section 76.924 of the Rules. That section provides a hierarchy for transfer prices between cable operators and their affiliates. Where the invoice price is determined by a prevailing company price, that price shall be used. A prevailing company price exists when there has been a "substantial number" of like transactions with nonaffiliates. The existence of a "substantial number" of arms-length transactions with non-affiliates provides adequate assurance that the transfer price reflects fair market value.

In the absence of a prevailing company price, the existing rules require that services provided between affiliates shall be priced at "cost". The Commission has previously recognized that "cost" provides a reasonable surrogate for market price where it is impractical to obtain a direct estimate of market value.⁶ For asset transfers, the existing rules require that assets transferred into

⁵ FNPRM at paras. 262 et seq.

⁶ See, e.g., AT&T Information Systems v. FCC, 854 F.2d 1442, 1446-47 (D.C. Cir. 1988); In the Matter of Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services (Second Computer Inquiry), 6 FCC Rcd 6066 (1991).

regulation be priced at the lower of cost or fair market value. Assets transferred out of regulation are priced at the higher of cost or fair market value. These asymmetrical rules result in a systematic benefit to the regulated operations.⁷ BellSouth believes that these rules are more than adequate to protect consumers from abusive behavior in the area of affiliate transactions.

In the notice portion of the FNPRM, the Commission proposes to impose on cable operators the far more onerous affiliate transaction rules proposed for telephone companies in the Telco Notice.⁸ The limited additional protection that the public would derive from the proposed rules does not begin to justify the massive additional burden that the proposed rules would impose.

Most of the increase in administrative costs comes from two of the proposals in the FNPRM: the proposal to curtail severely the use of prevailing company price as a valuation method; and the proposal to apply the present asset transfer rules to the provision of services.⁹ The former proposal

⁷ BellSouth has advocated the elimination of the asymmetrical asset transfer rules applicable to telephone companies. BellSouth likewise believes that the existing asset transfer rules applicable to cable operators go beyond what is necessary to provide adequate consumer protection.

⁸ Amendment to Parts 32 and 64 of the Commission's Rules to Account for Transactions between Carriers and Their Nonregulated Affiliates, Notice of Proposed Rulemaking, CC Docket No. 93-251, 8 FCC Rcd 8071 (1993) ("Telco Notice"). FNPRM at para. 261, n.519.

⁹ FNPRM at para. 309.

will increase administrative costs by increasing the number of transactions that will be valued using the more cumbersome default standard. The application of the present asset transfer rules to services will require that the cable operator determine not only the cost of such services, but also their estimated fair market value. In the context of asset transfers, this requirement is manageable, although burdensome, because physical assets can be valued using fairly straightforward and generally understood methodologies. By contrast, services are provided to affiliates on a far more frequent basis, and there are no comparable, widely available methodologies for determining the fair market value of most services. Thus, the curtailment of prevailing company prices and the extension of the present asset transfer rules to services will greatly increase costs and uncertainty to cable operators.

In response to the Telco Notice, BellSouth retained Theodore Barry & Associates ("TB&A") to evaluate the feasibility of obtaining estimated fair market value ("EFMV") analyses for services transactions, as would be required under the proposed rules for affiliate transactions. TB&A concluded that the proposed rules were unnecessary, impractical, and prohibitively expensive. True estimates of fair market value would not be available for most service-based affiliate transactions as the majority involve knowledge-based transactions for which equivalents

in the market place are non-existent or surrogates are difficult to find. Furthermore, the cost to acquire EFMV for services transactions would be prohibitive. TB&A estimates that the predominant knowledge-based transactions would cost \$70,000 per evaluation per transaction. The less difficult EFMV for transaction-based services would cost an estimated \$40,000 per evaluation per transaction. Finally, the output of the EFMV analyses would be inherently unreliable as a consistent method would not be feasible due to the variety of possible evaluation methods for the diverse array of services evaluated.

TB&A conservatively estimated a portion of the recurring annual cost to BellSouth and its affiliates to meet the EFMV study requirement of the proposed rules to be \$14.4 million. This estimate did not include the initial "one-time" implementation costs, the increased internal costs needed to monitor the new process, or the cost of lost efficiencies from a reduction in beneficial affiliate transactions. The actual cost burden of the proposed rules would be significantly higher than the amount quantified by TB&A. Despite this huge cost burden, TB&A was unable to identify any tangible benefit to customers associated with the proposed rules.

The application of these proposed rules to cable operators makes no more sense than their application to telephone companies. The rules changes proposed in the

FNPRM would require cable operators to incur massive new administrative costs that would not result in any increase in output. Hence, they would reduce the productivity of cable operators and increase their costs without any noticeable consumer benefit. As such, the proposed rules are inconsistent with the Commission's overall regulatory goals and the public interest.

In addition to the burden on the cable operators, adoption of the proposed rules would impose substantial new costs on the Commission and the public. The FNPRM provides no guidance on how cable operators are to estimate fair market value of services. In the absence of clear standards, there is certain to be disagreement between the cable operators and the Commission staff on methodologies, procedures and results. Such uncertainty inevitably imposes additional requirements for staff resources at the Commission. At a time when Commission staff resources are already strained, the adoption of rules that will further burden those resources should be avoided unless clearly necessary to fulfill the Commission's responsibilities to the public. As demonstrated above, this is not such a case. Both the cable operators and the Commission will incur substantial cost increases with little, if any, public benefit.

In the FNPRM, the Commission proposes to adopt an accounting system for cable television operators that is a

simplified version of the Commission's current Part 32 rules applicable to telephone companies. The Commission also proposes to exempt from these requirements companies that are currently required to maintain their accounts in accordance with Part 32.¹⁰ BellSouth concurs with the Commission's conclusion that a simplified version of the Part 32 Rules will provide the basic accounting data necessary to implement cost-of-service regulation, and that companies that are required to maintain their accounts in conformance with Part 32 should not have to maintain separate accounting systems for their telephone and cable operations.

In the FNPRM, the Commission determined that it need not prescribe depreciation rates for cable television companies.¹¹ This is an area where regulatory parity between cable television companies and telephone companies is critical. With the convergence of technologies and the emerging competition between these industries, a regulatory regime in which cable television companies are free to recover their capital on a timely basis subject only to regulatory oversight, while telephone companies are saddled

¹⁰ FNPRM at para. 308.

¹¹ FNPRM at para. 133. "Further, we believe a depreciation prescription requirement would impose unjustified burdens without providing a balancing benefit to subscribers. Instead, regulators will closely monitor industry depreciation practices and carefully review depreciation showings in individual cost proceedings to assure that these depreciation practices are reasonable."

by regulators with costly, untimely and inadequate depreciation practices, is patently contrary to the public interest.

The FNPRM discusses the "price cap carrier option" adopted by the Commission for AT&T (but not for the price cap LECs) in the Simplification Order.¹² BellSouth has pending before the Commission a Petition for Reconsideration of the Simplification Order, in which BellSouth requests that the "price cap carrier option" be extended to the price cap LECs. The Commission's determination in this proceeding that the public interest does not require that it regulate the depreciation rates of cable television companies -- even those subject to cost-of-service regulation -- highlights

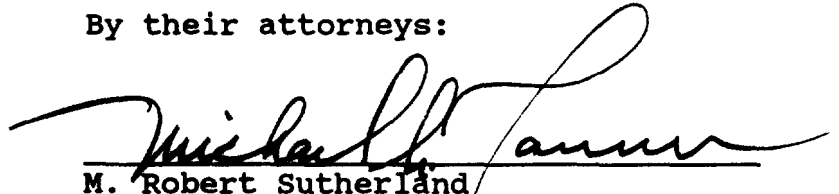
¹² Simplification of the Depreciation Prescription Process, Report and Order, 8 FCC Rcd 8025 (1993) ("Simplification Order").

the error committed in the Simplification Order. Rather than impose unnecessary regulation on the cable television industry, BellSouth urges the Commission to achieve regulatory parity by eliminating unnecessary regulation of LEC depreciation rates on reconsideration of the Simplification Order.

Respectfully submitted,

BELLSOUTH CORPORATION AND
BELLSOUTH TELECOMMUNICATIONS, INC.

By their attorneys:

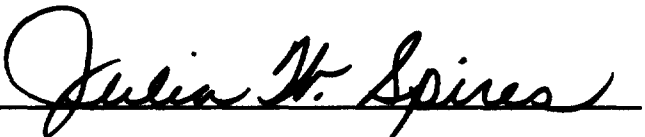
A handwritten signature in black ink, appearing to read "Michael A. Tanner", is written over a horizontal line.

M. Robert Sutherland
Michael A. Tanner
4300 Southern Bell Center
675 West Peachtree Street, N.E.
Atlanta, Georgia 30375
404 529-3854

July 1, 1994

CERTIFICATE OF SERVICE

I hereby certify that I have this 1st day of July, 1994, serviced all parties to this action with a copy of the foregoing COMMENTS reference to MM Docket No. 93-215 and CS Docket No. 94-28, by placing a true and correct copy of the same in the United States Mail, postage prepaid, addressed to the parties as set forth on the attached service list.


Julia W. Spires

Mr. David B. Gluck
Mr. Mark R. Boyes
Affiliated Regional
Communications, Ltd.
600 Las Colinas Boulevard
Suite 2200
Irving, Texas 75039

Robert S. Lemle, Esq.
Senior Vice President and
General Counsel
Cablevision Systems Corp.
One Media Crossways
Woodbury, New York 11797

Mark J. Palchick, Esq.
Baraff, Koerner, Olender &
Hochberg
5335 Wisconsin Avenue, N.W.
Suite 300
Washington, D.C. 20015-2003

John I. Davis, Esq.
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, D.C. 20006

Donna C. Gregg, Esq.
Michael Baker, Esq.
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, D.C. 20006

Robert L. James, Esq.
Cole, Raywid & Braverman
1919 Pennsylvania Ave., N.W.
Suite 200
Washington, D.C. 20006

Howard J. Symons, Esq.
Leslie B. Calandro, Esq.
Mintz, Levin, Cohn, Ferris
Glovsky and Popeo
701 Pennsylvania Avenue, N.W.
Suite 900
Washington, D.C. 20004

Lex J. Smith, Esq.
Alan H. Blankenheimer, Esq.
Joel W. Nomkin, Esq.
Brown & Bain
2901 North Central Avenue
Post Office Box 400
Phoenix, Arizona 85001-0400

Mr. Spencer R. Kaitz
Mr. Jerry Yanowitz
Mr. Jeffrey Sinsheimer
California Cable Television
Association
4341 Piedmont Avenue
Oakland, California 94611

John R. Feore, Jr., Esq.
David J. Wittenstein, Esq.
Dow, Hones & Albertson
1255 23rd Street, N.W.
Suite 500
Washington, D.C. 20037

Aaron I. Fleischman, Esq.
Stuart F. Feldstein, Esq.
Matthew D. Eumer, Esq.
Fleischman and Walsh
1400 Sixteenth Street, N.W.
Washington, D.C. 20036

Community Antenna Television
Association, Inc.
3950 Chain Bridge Road
P. O. Box 1005
Fairfax, Virginia 22030-1005

Brenda L. Fox, Esq.
Peter F. Feinberg, Esq.
J. G. Harrington, Esq.
Peter C. Godwin, Esq.
Dow, Lohnes & Albertson
1255 23rd Street, N.W.
Suite 500
Washington, D.C. 20037

Mr. Robert Sachs
Mr. Howard B. Homonoff
Continental Cablevision, Inc.
The Pilot House
Lewis Wharf
Boston, Massachusetts 02110

Richard E. Wiley, Esq.
Philip V. Permut, Esq.
Peter D. Ross, Esq.
Rosemary C. Harold, Esq.
Wiley, Rein & Fielding
1776 K Street, N.W.
Washington, D.C. 20006

Stephen R. Ross, Esq.
Kathryn A. Hutton, Esq.
Ross & Hardies
888 Sixteenth Street, N.W.
Suite 300
Washington, D.C. 20006-4103

Trudi McCollum Foushee, Esq.
Vice President - Legal
Crown Media, Inc.
One Galleria Tower
13355 Noel Road, Suite 1650
Dallas, Texas 75240

Robert L. Hoegle, Esq.
Timothy J. Fitzgibbon, Esq.
Carter, Ledyard & Milburn
1350 I Street, N.W.
Suite 870
Washington, D.C. 20005

James E. Meyers, Esq.
Baraff, Koerner, Olender
& Hochberg
5335 Wisconsin Avenue, N.W.
Suite 300
Washington, D.C. 20015-2003

John W. Pestle, Esq.
Varnum, Riddering, Schmidt
& Howlett
333 Bridge Street, N.W.
P. O. Box 352
Grand Rapids, MI 49501-0352

Eric E. Breisach, Esq.
Howard & Howard
107 W. Michigan Avenue
Suite 400
Kalamazoo, Michigan 49007

Mr. Ron D. Katznelson
Multichannel Communications
Sciences, Inc.
5910 Pacific Center Boulevard
San Diego, California 92121

Judith A. McHale, Esq.
Barbara S. Wellbery, Esq.
Discovery Communications, Inc.
7700 Wisconsin Avenue
Bethesda, Maryland 20814

Norman M. Sinel, Esq.
Patrick J. Grant, Esq.
Stephanie M. Phillips, Esq.
William E. Cook, Esq.
Arnold & Porter
1200 New Hampshire Ave., N.W.
Washington, D. C. 20036

Donna C. Gregg
Wiley, Rein & Fielding
Counsel for Bend Cable, et al
1776 K Street, N.W.
Washington, D.C. 20006

Paul J. Berman, Esq.
Alane C. Weikel, Esq.
Covington & Burling
1201 Pennsylvania Ave., N.W.
P. O. Box 7566
Washington, D.C. 20044

Robert Corn-Revere, Esq.
Jacqueline P. Cleary, Esq.
Hogan & Hartson
555 13th Street, N.W.
Washington, D.C. 20004

Mr. Robert Weisberg
Mountain Cablevision, Inc.
145 E. 92 Street (PHA)
New York, New York 10128

Peter Tannenwald, Esq.
Kathleen L. Franco, Esq.
Arent, Fox, Kitner, Plotkin
& Kahn
1050 Connecticut Avenue, N.W.
Washington, D.C. 20036-5339

Janice L. Lower, Esq.
Michael R. Postar, Esq.
Duncan, Weinberg, Miller
& Pembroke
1615 M Street, N.W.
Suite 800
Washington, D.C. 20036

Mr. Frederick Kuperberg
Ms. Maureen Whalen
The Disney Channel
3800 West Alameda Avenue
Burbank, California 91505

Ms. Ruth C. Rodger
Executive Director
Home Recording Rights
Coalition
2300 N Street, N.W.
Washington, D.C. 20037

Daniel L. Brenner, Esq.
NCTA
1724 Massachusetts Ave., N.W.
Washington, D.C. 20036

Mr. Matthew York
Videomaker Magazine
P.O. Box 4591
920 Main Street
Chico, California 95927

Charles S. Walsh, Esq.
Seth A. Davidson, Esq.
Mark J. O'Connor, Esq.
Fleischman and Walsh
1400 Sixteenth Street, N.W.
Suite 600
Washington, D.C. 20036

Mr. Joseph J. Albarella
Cable TV of Jersey City, Inc.
800 Rahway Avenue
Union, New Jersey 07083

Ms. Judith L. Neustadter
Paradise Television Network
2200 Main Street, Suite 611
P.O. Box 2252
Wailuku, Maui, Hawaii 96793

Mr. Bradley Stillman
Mr. Gene Kimmelman
Consumer Federation of America
1424 16th Street, N.W.
Suite 604
Washington, D.C. 20036

Mr. James A. Penney, Esq.
V.P. and General Counsel
Northland Communications Corp.
1201 3rd Avenue
Suite 3600
Seattle, Washington 98101

Mr. Robert Sutherland
Mr. Michael Tanner
BellSouth
Telecommunications, Inc.
4300 Southern Bell Center
675 West Peachtree St., N.E.
Atlanta, Georgia 30375

Mr. Jerry Parker
Superstar Connection
3801 S. Sheridan Road
Tulsa, Oklahoma 74145

General Instrument Corp.
1899 L Stret, N.W.
5th Floor
Washington, D.C. 20036

Mr. Bertram M. Carp
Turner Broadcasting
Systems, Inc.
820 First Street, N.E.
Washington, D.C. 20037-1420

Ward W. Wueste, Jr., Esq.
Marceil Worrell, Esq.
GTE Service Corporation
P.O. Box 152092
Irving, Texas 75015-2092

William R. Richardson, Jr., Esq.
Christopher M. Heiman, Esq.
Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, D.C. 20037-1420

Henry M. Rivera, Esq.
Ann Bavender, Esq.
Ginsburg, Feldman & Bress
1250 Connecticut Ave., N.W.
Washington, D.C. 20036

Matthew L. Leibowitz, Esq.
Joseph A. Belisle, Esq.
Leibowitz & Spencer
One S.E. Third Avenue
Suite 1450
Miami, Florida 33131

Ms. Barbara N. McLennan
Mr. George A. Hanover
Consumer Electronics Group
Electronics Industries Assoc.
2001 Pennsylvania Ave., N.W.
Washington, D.C. 20044

Martin T. McCue, Esq.
Linda Kent, Esq.
USTA
900 19th Street, N.W.
Suite 800
Washington, D.C. 20006-2105

Ronald A. Siegel, Esq.
Roy R. Russo, Esq.
J. Brian DeBoice, Esq.
Wometco Cable, et al.
Cohn and Marks
1333 New Hampshire Ave., N.W.
Suite 600
Washington, D.C. 20036

Mr. Stephen R. Ross
Ms. Kathryn A. Hutton
Intermedia Partners
888 16th Street, N.W.
Suite 300
Washington, D.C. 20006

Mr. J. Bruce Irving
Sur Corporation
Bailey, Hunt, Jones & Busto
Courvoisier Centre, Suite 300
501 Brickell Key Drive
Miami, Florida 33131-2623

Gardner F. Gillespie, Esq
Jacqueline P. Cleary, Esq.
Coalition of Small Systems
Operators, Prime Cable
555 13th Street, N.W.
Washington, D.C. 20015-2003

Mr. Roy A. Sheppard
Cable Services
Box 608
Jamestown, Maryland 58401-0608

Mr. John J. Sie
Mr. James E. Meyers
Encore Media Corporation
5335 Wisconsin Avenue, N.W.
Suite 300
Washington, D.C. 20015-2003

Janet Reno, Esq.
Attorney General
Department of Justice
10th Street & Constitution Ave.
Room 5111
Washington, D.C. 20530

Mr. David Cosson
Ms. L Marie Guillory
National Telephone Cooperative
Association
2626 Pennsylvania Ave., N.W.
Washington, D.C. 20037

Mr. William F. Caton, Sec.
Federal Communications
Commission
1919 M Street, N.W.
Room 222
Washington, D.C. 20554

Mr. Jud Colley
President
Community Broadcasters
Association
P.O. Box 191229
Dallas, Texas 75219

Mr. Thomas J. Halicki
National Assoc. of Towns
and Townships
1522 K Street, N.W.
Suite 600
Washington, D.C. 20005

Michael E. Glover, Esq.
Bell Atlantic
1710 H Street, N.W.
Washington, D.C. 20006

Mr. J. Dale Haslett
Alsea River Cable TV
P.O. Box 386
Waldport, Oregon 97394

Angela J. Campbell, Esq.
Sharon L. Webber, Esq.
Center for Media Education
Institute for Public Rep.
Georgetown University Law Ctr.
600 New Jersey Avenue, N.W.
Washington, D.C. 20001

Mr. James Johnston
1133 Connecticut Ave., N.W.
Suite 1000
Washington, D.C. 20036

Mr. Jeff Treeman
United Video, Inc.
3801 S. Sheridan Road
Tulsa, Oklahoma 74145

Office of General Counsel
Federal Communications
Commission
1919 M Street, N.W.
Room 614
Washington, D.C. 20554

David A. Irwin, Esq.
Irwin, Campbell & Crowe
1320 18th Street, N.W.
Suite 400
Washington, D.C. 20036

Ms Janet Wigfield
City of St. Paul
Cable Communications Officer
68 City Hall
15 W. Kellogg Boulevard
St. Paul, Minnesota 55102

Mr. Michael E. Turner
Televista Communications
37269 Huron River Drive
P.O. Box 604
New Boston, Michigan 48164

Ms. Deborah Jacobson
Bank of New York
One Wall Street
16th Floor
New York, New York 10286

Ian D. Volner, Esq.
Venable, Baetjer, Howard
& Civiletti
1201 New York Ave., N.W.
Suite 1000
Washington, D.C. 20005

Bruce Collins, Esq.
C-Span
Legal Counsel
400 North Capital St., N.W.
Suite 650
Washington, D.C. 20001

Maurita K. Coley, Esq.
V.P., Legal Affairs
Black Entertainment Television
1232 31st Street, N.W.
Washington, D.C. 20007

Mr. Paul V. Engle
Engle Broadcasting
104 Bellvue Avenue
Hammononton, New Jersey 08037

Mr. Clifford K. Higa
Director of Commerce and
Consumer Affairs
State of Hawaii
1010 Richards Street
Honolulu, Hawaii 96813

Philip L. Verveer, Esq.
Sue D. Blumenfeld, Esq.
Laurence D. Atlas, Esq.
Melissa Newman, Esq.
Wilkie, Farr & Gallagher
Three Lafayette Centre
Suite 600
1155 21st Street, N.W.
Washington, D.C. 20036-3384

ITS, Inc.
1919 M Street, N.W.
Room 246
Washington, D.C. 20554

L. Charles Keller
Pepper & Corazzini
Counsel for Eternal Word
200 Montgomery Building
1776 K Street, N.W.
Washington, D.C. 20006

Edward Schor
Viacom International
1515 Broadway
New York, N.Y. 10036

William Wolfson
Asst Corp Counsel
Law Department
City of Detroit
1010 City-County Building
Detroit, MI 48226